United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

75-1108

To be argued by
JOHN C. SABETTA

United States Court of Appeals

FOR THE SECOND CIRCUIT

Docket No. 75-1108

UNITED STATES OF AMERICA,
Appellee,

—v.—

ROBERT S. PERSKY,
Defendant-Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR THE UNITED STATES OF AMERICA

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Preliminary Statement

Robert S. Persky appeals from a judgment of conviction entered on January 23, 1975, in the United States District Court for the Southern District of New York after a nine day trial before the Honorable Inzer B. Wyatt, United States District Judge, and a jury, and from an order of February 28, 1975 denying his motion for a directed verdict of acquittal, an order in arrest of judgment and a new trial.

Indictment 73 Cr. 192, filed March 1, 1973, contained 12 counts, two of which, Counts Four and Five, were the subject of the trial and related proceeding from which

this appeal is taken.* Count Four charged Persky and co-defendants Morton S. Kaplan and Ramon N. D'Onofrio with fraud in connection with the purchase and sale of the common stock of Microthermal Applications, Inc. ("Microthermal"), a public company, in violation of Title 15, United States Code, Section 78j(b), and Rule 10b-5 (17 C.F.R. § 240.10b-5), and Title 18, United States Code, Section 2. Count Five charged Persky and Kaplan with the failure to file with the SEC in behalf of Microthermal a required current report on Form 8-K, in violation of Title 15, United States Code, Sections 78o and 78ff and Rule 15d-11 (17 C.F.R. § 240.15d-11), and Title 18, United States Code, Section 2.

Trial of Persky as to Counts Four and Five began on January 13, 1975 and ended on January 23, 1975 when the jury returned a verdict of guilty as to Count Four.** That same day Judge Wyatt sentenced Persky to a two year term of imprisonment, three months to be served and the balance suspended, to be followed by two years

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* Counts Four and Five were severed in 1973 from the earlier trial of defendants Persky, Philip Zane and Jerome E. Silverman on the other ten counts of Indictment 73 Cr. 192 in which they, variously, were named along with Morton S. Kaplan and Charles J. Fischer. That trial resulted in the convictions of Persky, Zane and Silverman on Count Two, which charged them with filing with the SEC in behalf of Microthermal Applications, Inc. a false annual report Form 10-K, in violation of Title 15, United States Code, Sections 78o and 78ff and 17 C.F.R. §§ 240.15d-1 and 240.12b-20. Those convictions were affirmed *sub nom. United States* v. *Zane*, 495 F.2d 683 (2d Cir.), *cert. denied*, 419 U.S. 895 (1974).

Defendants Kaplan and D'Onofrio pled guilty to Counts One and Four, respectively, of the instant indictment, and D'Onofrio testified as a government witness at the trial which is the subject of this appeal. Defendant Fischer pled guilty to superseding Information 75 Cr. 28. All have since been sentenced by Judge Wyatt.

** A judgment of acquittal as to Count Five had been entered by Judge Wyatt at the close of the government's direct case.

probation—the term of imprisonment to run concurrently with a four month prison term Persky was then serving as a result of his earlier conviction of Count Two. Both terms of imprisonment have since been served.

On February 21, 1975 Persky moved the District Court, pursuant to Rules 12, 29, 33 and 34 of the Federal Rules of Criminal Procedure, for a judgment of acquittal, an order in arrest of judgment and a new trial. That motion, premised on legal arguments already once rejected by the District Court during the trial, was denied by Judge Wyatt in a memorandum endorsement dated February 28, 1975.

Statement of Facts

A. Synopsis

The government's proof established that beginning with the spring of 1970, and for approximately one year thereafter, defendant Robert S. Persky, the attorney and secretary of Microthermal, a public company, together with others engaged in a course of conduct designed to conceal from the public, Microthermal's stockholders and the authorities the fact that $480,000 of the approximately $700,000 Microthermal had raised in its only public offering in July 1969 had been misapplied and lost.

To that end, Persky and others caused Microthermal to enter into a sequence of sham asset acquisition and merger transactions. In the execution of those transactions, and at a time when Microthermal's stock was daily being traded in the public over-the-counter market, Persky, and others at his direction, made materially false statements, in notices to stockholders and in corporate press releases disseminated to the financial media, to the effect that Microthermal would and did have assets which included $375,000. In truth, as Persky well knew, those moneys had been misapplied and long since lost by persons other than himself.

B. The Government's Case

In July 1969, in its sole offering to the public, Microthermal sold 200,000 shares of its common stock at $4.00 per share, which after expenses netted the company approximately $700,000 (Tr. 614; GX 8, 44).* Microthermal's stock was thereafter publicly traded in the over-the-counter market until at least some time in 1971 (Tr. 177-78, 384, 763, 900; GX 64, 65).

Subsequent to the public offering in 1969, Morton S. Kaplan, Microthermal's President, controlling stockholder and originally its sole employee, in order to obtain assistance in promoting Microthermal and his other companies, established a relationship with Takara Partners ("Takara"), a hedge fund in New York City dealing in securities, whose general partners and investment advisors were John Peter Galanis and Akiyoshi Yamada (Tr. 105-110).

In October 1969 and again in January 1970, Kaplan caused Microthermal to transfer to Takara payments of $240,000, for a total of $480,000 (Tr. 108-09, 118). These moneys, transferred without limitation on their use, were soon dissipated by Galanis and Yamada, who used them to defray Takara's expenses and repay its creditors and to invest in illiquid securities (Tr. 108-10, 126).

On numerous occasions between October 1969 and July 1970, Galanis and Yamada had conversations with Persky, Microthermal's secretary and attorney, and Kaplan. Those conversations established that all parties concerned knew

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* The trial transcript is abbreviated herein as "Tr." and Government Exhibit as "GX".

At the time of this public offering, Microthermal was a new venture with no operating history (GX 8). It did not thereafter ever develop any operational facilities or market any product (Tr. 615).

that the $480,000 transferred to Takara in October 1969 and January 1970 had been used by this hedge fund not to purchase certificates of deposit for Microthermal but, rather, had been expensed or invested by Takara in violation of the "Application Of Proceeds" section of Microthermal's prospectus—a section which Persky had helped draft (Tr. 1022) and which had been disseminated to the public at the time of the public offering (Tr. 115-25, 132-36).* That section of the prospectus provided that funds remaining after expenses and specific allocations by management would be placed in certificates of deposit, government bonds or other interest bearing obligations (GX 8).

Despite demands by Kaplan and Persky on Takara for the return of the $480,000, by spring of 1970 Takara had repaid only a portion, leaving still unpaid approximately $375,000 (Tr. 131-32). Persky, recognizing that Microthermal would soon be required to file with the SEC an annual report Form 10-K containing certified financials, and apprehensive about his liability as corporate secretary and legal counsel for the $480,000 dissipated by Galanis and Yamada, knowingly undertook in the spring and summer of 1970 to conceal the disappearance of those moneys (Tr. 125, 136). Microthermal's then accountants, Arthur Andersen & Co., were fired and replaced by more flexible accountants, Zane and Silverman; and elaborate machinations were employed by Persky and others to obtain false and fraudulent bank documents designed to create the fictitious impression that Microthermal had purchased a bearer certificate of deposit in the amount of $500,000. Thereafter Zane and Silverman, in ostensible reliance on

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* Virtually all of Microthermal's corporate documents were prepared by or at the direction of Persky, and were maintained at the offices of the approximately 30 man, Manhattan law firm of which Persky, who specialized in securities law, was a member (Tr. 228, 616; GX 28).

the evidence of Microthermal's purported purchase of the $500,000 certificate of deposit, certified a statement of Microthermal's assets, as of January 31, 1970, which under "Current Assets" contained an entry for "Cash and cash items" of $525,024 (Tr. 139, 142-47, 469, 631-35, 748-54; GX 9). That certified and false statement of assets was included in Microthermal's Form 10-K filed with the SEC by Persky and others in July 1970 (Tr. 147-49; GX 33).*

Following that false filing with the SEC, Persky told Galanis that he was tired of having the problem of the misapplied $480,000 on his and Kaplan's shoulders. He suggested that Galanis and Yamada find a way to merge away Microthermal and the problem (Tr. 168-69). Galanis thereafter induced Robert Hagopian, who controlled Meridian Capital Corporation ("Meridian Capital"), a cash poor and closely held corporation in San Francisco engaged in the securities business, to agree to such a merger (Tr. 169-74, 386-95). An agreement was prepared by L. Martin Gibbs, a young law associate of Persky working under his direction and supervision, and was later signed on August 13, 1970. It provided for a closing on October 26, 1970 to be conditioned upon, among other things, the approval of the shareholders of Microthermal and Meridian Capital (Tr. 397, 771-78; GX 27A).**

On August 14, 1970, Gibbs, under Persky's direction and supervision, prepared and sent to various financial

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* It was this false filing which was the basis of Count Two, of which Persky, Zane and Silverman were convicted at the first trial.

** The agreement provided that Meridian Capital would sell to Microthermal all of its assets subject to substantially all of its liabilities, in exchange for a substantial number of newly authorized and issued shares of Microthermal sufficient to give the then principals of Meridian Capital control of Microthermal. Following the transaction Microthermal was to change its name to Meridian Capital (Tr. 393-95).

media, including the *New York Times, The Wall Street Journal*, Dow Jones and the wire services (Tr. 779-81; GX 28), a press release announcing the substance of Microthermal's agreement with Meridian Capital. That release, reviewed by Persky prior to issuance, stated in accordance with the terms of the agreement that prior to the closing Microthermal would transfer all of its operating assets subject to substantially of its liabilities, except for approximately $375,000 which was to remain in Microthermal, to Waltech Corp., a wholly owned subsidiary of Microthermal; and that Waltech Corp. would then be spun off to the shareholders of Microthermal on a share for share basis. In truth, following the proposed transfers to Waltech Corp. Microthermal, rather than having $375,000 in liquid assets, would and was to be little more than a shell of a public company—with virtually no assets and no liabilities. That false and misleading August 14, 1970 press release was published in its entirety in the O.T.C. Market Chronicle on August 27, 1970 (Tr. 960; GX 79).

On October 9, 1970 Persky, over his name as corporate secretary, caused a notice to be sent to all record holders of Microthermal stock announcing a special meeting of stockholders to be held on October 20, 1970 at the offices of Persky's firm (Tr. 783; GX 62, 66). One of the purposes of that meeting as stated in the notice was:

> "4. To consider and approve the transfer of substantially all of the operating assets, except for approximately $375,000, of the Company, subject to substantially all the liabilities of the Company, to a wholly-owned subsidiary of the Company, Waltech Corporation, and the distribution of the shares of Waltech Corporation to the shareholders of the Company on the basis of one share of Waltech Corporation for each issued and outstanding share of the Company." (GX 66)

A few days prior to October 15, 1970, Hagopian of Meridian Capital concluded from a conversation he had with Galanis that the $375,000 in assets supposedly held by Microthermal in the form of a certificate of deposit did not exist (Tr. 396). He advised Galanis and later Persky that under the circumstances Meridan Capital would not consummate the agreement with Microthermal (Tr. 403-05, 411). Hagopian agreed, however, not to publicize the true reason for Meridian Capital's unwillingness to close, but to declare instead that Meridan Capital was unable to perform one of the conditions precedent under the terms of the agreement (Tr. 408; GX 31).*

Persky himself, even prior to word of Meridian Capital's refusal to close, had had growing doubts as to whether the proposed transaction with Meridian Capital would serve to cover over permanently the fact that approximately $375,000 of Microthermal's money had been lost (Tr. 185-88). In the face of those doubts and Meridian Capital's already expressed refusal to close, Persky nonetheless instructed Gibbs to conduct the stockholders meeting as scheduled. Accordingly, at a meeting on October 20, 1970, attended by a few stockholders, including one Lloyd Albin, the agreement between Microthermal and Meridian Capital, and the Waltech spin-off, were approved (Tr. 783-85).

Although the agreement with Meridian Capital, which had been approved, was never consummated, the stockholders received no notice of that fact nor, of course, of the fact that Microthermal did not have $375,000 in assets as represented. Indeed, on November 30, 1970 Lloyd Albin purchased in the open market an additional 1,000 shares of

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* Hagopian had by then received from Galanis, in connection with certain other criminal activities, approximately $500,000 in bribes (Tr. 173).

Microthermal stock, which he would not have purchased had he known the true condition of Microthermal's assets (Tr. 761-67; GX 69D).

On October 23, 1970, another press release was prepared by Gibbs under Persky's supervision and sent with Persky's knowledge to all Microthermal stockholders. (Tr. 607; GX 63, 89). It announced in part that:

> "Micro has transferred substantially all of its assets, except $375,000, to Waltech Corporation and Waltech Corporation has assumed substantially all the liabilities of Micro." (GX 89)*

In late September 1970, pursuant to Persky's urgings, Galanis began to seek another, more suitable merger candidate for Microthermal (Tr. 190). In so doing, he sought out Ramon D'Onofrio, a man who had assisted him in the criminal manipulation of numerous securities and who controlled a small, closely held corporation called U.S. Secretarial Institute, Ltd. ("U.S. Secretarial"). D'Onofrio agreed, for a fee of $50,000 paid to him by Galanis, to cause U.S. Secretarial, which was essentially worthless,** to issue to Microthermal 315,000 shares, or 49 per cent, of its stock (Tr. 206-210, 480, 781-83, 807-816; GX 19, 43) in exchange for, purportedly, a bearer form $375,000 certificate of de-

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* As evidenced by Government Exhibit 89, a copy of that press release was also sent by Persky to the National Association of Securities Dealers.

** U.S. Secretarial was begun in 1969 with an initial capitalization of $30,000. By the end of September 1970, it had lost more than $17,000, had liabilities in excess of assets of more than $5,000 and had witnessed a change in United States immigration laws which undermined its principal reason for being (Tr. 545-50, 555; GX 21, 39).

posit owned by Microthermal.* An agreement to that effect was drafted by Gibbs, under Persky's direction and supervision.

On or shortly after November 20, 1970, at the offices of Persky's law firm, the agreement was consummated (Tr. 833, 1119-27). A representative of U.S. Secretarial received an empty envelope, purportedly containing a $375,000 bearer form certificate of deposit, in exchange for a certificate of 315,000 shares of U.S. Secretarial stock. At the transaction's conclusion, Microthermal's assets consisted of 315,000 shares of U.S. Secretarial and 2,500 shares of Waltech (Tr. 489-92, 1122-27).

In March 1971, in an effort to oust themselves of any continuing affiliation with and responsibility for Microthermal, Persky and Kaplan merged Microthermal with Continental Engineering and Development, Inc. ("Continental Engineering"), a small, closely held corporation in Washington which was seeking to merge with a public shell —that is, a company with no assets and no liabilities whose shares were widely held and could be publicly traded.** As a result of the merger, the locus and control of Microther-

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* As originally proposed, Microthermal and U.S. Secretarial were to engage in a reverse acquisition where, by means of a stock for stock exchange, U.S. Secretarial would become a wholly owned subsidiary of Microthermal and the former principals of U.S. Secretarial would become the new control persons of Microthermal. The purported, but in truth non-existent, $375,000 certificate of deposit supposedly a part of Microthermal's assets was, under the plan, later to be expensed away on various offshore enterprises. This plan was abandoned when Persky apparently realized that it might require the approval of Microthermal's stockholders and another stockholders' meeting (Tr. 200-05, 469-75).

** In that transaction, no value was attributed by Persky or Microthermal to the 315,000 shares of U.S. Secretarial held by Microthermal, which purportedly had been purchased on November 20, 1970 with a $375,000 certificate of deposit (Tr. 996-98).

mal shifted over 3,000 miles to the State of Washington to the former principals of Continental Engineering.* The stock of the surviving entity known as Microthermal apparently became worthless (Tr. 834-45, 959, 984-98).

C. The Defense Case

Persky did not testify.

His wife, Marilyn Persky, testified that she and her husband still held the shares of Microthermal they had purchased in July 1969 in the public offering and those which Persky had received thereafter as a fee. She also testified she and Persky were abroad on a vacation for 17 days in July 1970 (Tr. 1095-98).

William Jarblum, Persky's law partner, testified in effect that a newspaper clipping pertaining to U.S. Secretarial, which was among several D'Onofrio had identified as ones he had shown to Persky at an incriminating meeting between them in October 1970, had once borne the handwritten name of the newspaper from which it had been taken and a date of January, 1971 (Tr. 1091-93).

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* Although the merger was consummated in March 1971, Persky caused the merger agreement and its supposed closing date to be back dated to November 20, 1970 (Tr. 841-45; GX 49).

ARGUMENT

POINT I

Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder are not unconstitutionally vague.

Persky contends that Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 thereunder, are unconstitutionally vague on their face and therefore void.* The contention is without merit.

The constitutional attack on Section 10(b) and Rule 10b-5 on vagueness grounds was long ago rejected as "shop worn." *Speed* v. *Transamerica Corp.*, 99 F. Supp. 808, 831-32 (D. Del. 1951). This Court has said that Rule 10b-5 "was validly promulgated." *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783, 786 (2d Cir. 1951); *accord*, *Hooper* v. *Mountain States Securities Corp.*, 282 F.2d 195, 200-01 (5th Cir. 1960), *cert. denied*, 365 U.S. 814 (1961); *United States* v. *Shindler*, 173 F. Supp. 393, 394-95 (S.D.N.Y. 1959). See also *Nemitz* v. *Cunny*, 221 F. Supp. 571, 574-75 (N.D. Ill. 1963). And the Section and Rule have served as judicially approved predicates in cases whose number is legion, including private actions for damages, enforcement proceedings and criminal prosecutions, without even intimation that either the Section or Rule, or both, may be void for vagueness.

Void-for-vagueness attacks on Section 10(b) and Rule 10b-5 have apparently been few in number and judicial treatment of the same exceedingly rare. The language of Rule 10b-5, however, is substantially the same as that

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* The Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78hh (1970), is hereinafter sometimes cited as "1934 Act".

found in Section 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a).* The latter general fraud provision has repeatedly been held to be constitutional in both its penal and civil applications, and in the face of void-for-vagueness attacks. *Coplin* v. *United States*, 88 F.2d 652, 656-58 (9th Cir.), *cert. denied*, 301 U.S. 703 (1937); *Jones* v. *SEC*, 79 F.2d 617 (2d Cir. 1935), *rev'd on other grounds*, 298 U.S. 1 (1936); *SEC* v. *Jones*, 85 F.2d 17 (2d Cir.), *cert. denied*, 299 U.S. 581 (1936); *McMann* v. *Engel*, 16 F. Supp. 446, 447 (S.D.N.Y. 1936), *aff'd*, 87 F.2d 377 (2d Cir.), *cert. denied*, 301 U.S. 684 (1937); *United States* v. *Bogy*, 16 F. Supp. 407 (W.D. Tenn. 1936); *SEC* v. *Torr*, 15 F. Supp. 315, 318 (S.D.N.Y. 1936), *rev'd on other grounds*, 87 F.2d 446 (2d Cir. 1937).

Other of the general SEC fraud provisions, certain of whose language is much akin to portions of the Section and Rule challenged here, have been upheld against similar void-for-vagueness attacks. *Charles Hughes & Co. Inc.* v. *SEC*, 139 F.2d 434, 436 (2d Cir. 1943), *cert. denied*, 321 U.S. 786 (1944) (Section 15 (c)(1) of the 1934 Act, and Rule 15c1-2 thereunder); *United States* v. *Pope*, 189 F. Supp. 12, 22 (S.D.N.Y. 1960) (Weinfeld, *J.*) (Section 32a, and Rule 14a-9 under Section 14(a), of the 1934 Act). See also *Roberts* v. *United States*, 226 F.2d 464 (6th Cir. 1955), *cert. denied*, 350 U.S. 935 (1956) (wire fraud statute, 18 U.S.C. 1343, not unconstitutional for vagueness).

In contrast to the foregoing, Persky has cited not a single authority which suggests even in *dicta*, much less holds, that Section 10(b) and Rule 10b-5 are void for vagueness. Nor has he specified what language of the Sec-

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* Rule 10b-5 "was patterned upon the language of § 17(a) of the Securities Act of 1933, 15 U.S.C.A. § 77q(a) but added words to cover fraud if perpetrated on sellers as well as purchasers." *Hooper* v. *Mountain States Securities Corp.*, *supra*, 282 F.2d at 201 n. 4.

tion and Rule was unconstitutionally vague and failed to provide him with sufficient notice of the proscribed conduct. Admittedly, as Persky contends, Section 10(b) and Rule 10b-5 have been given broad judicial application. But broadness of reach beyond rigid common law formulations, see generally *Charles Hughes & Co., Inc.* v. *SEC*, *supra*, 139 F.2d at 437, is not synonymous with unconstitutional vagueness.

The language and legislative history of the Securities Exchange Act of 1934 make clear that it was intended to cover "a wide field." H.R. REP. No. 1383, 73d Cong., 2d Sess. 6 (1934). It was enacted in response to the "speculative orgy of 1928 and 1929," S. REP. No. 1455, 73d Cong., 2d Sess. 81 (1934), and a presidential call for securities "legislation [that] has teeth in it." H.R. REP. No. 1383, 73d Cong., 2d Sess. 2 (1934). Congress recognized that "[s]peculation, manipulation, . . . investors' ignorance, and disregard of trust relationships by those whom the law should regard as fiduciaries" were "all a single seamless web," *id.* at 6, and that an act designed to purge all avenues of abuse would require broad remedial provisions.

This Court has said that the broad language of Rule 10b-5 "demonstrates that the SEC sought by the Rule . . . fully to implement the Congressional purpose and objectives underlying Section 10(b)." *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 860 (2d Cir. 1968) (en banc), *cert. denied sub nom. Coates* v. *SEC*, 394 U.S. 976 (1969); and further that:

> "We believe that § 10(b) and Rule 10b-5 prohibit *all* fraudulent schemes in connection with the purchase or sale of securities, whether the artifices employed involve a garden type variety of fraud, or present a unique form of deception. Novel or atypical methods should not provide immunity from the securities laws." (Emphasis in original.)

A.T. Brod & Co. v. *Perlow,* 375 F.2d 393, 397 (2d Cir. 1967); *accord, Superintendent of Insurance* v. *Bankers Life & Casualty Co.,* 404 U.S. 6, 11 n.7 (1971). See also *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128, 151 (1972).

Moreover, the fact that there have been a vast number of cases construing Section 10(b) and Rule 10b-5 does not, as Persky contends, somehow provide support for his claims of the constitutional infirmity of that Section and Rule. The accretion of that judicial gloss has served in fact to supply "considerable specificity by way of examples of the conduct which [the Section and Rule] cover", *Parker* v. *Levy,* 417 U.S. 733, 754 (1974), and thereby to augment the notice or warning provided to potential transgressors such as Persky.

Finally, whether one could hypothesize circumstances in which a defendant might have been unable to ascertain from the face of Section 10(b) and Rule 10b-5, because of putative vagueness, their applicability to his conduct—and hence that as applied to him they were unconstitutional and invalid—no such possibility obtained here. Persky, an experienced attorney who specialized in securities law, participated in 1970 in a scheme to conceal the misapplication and loss of approximately $375,000 of a public company's money. In the course of that scheme and at a time when the company's stock was daily being traded in the over-the-counter market, he published and widely disseminated materially false statements of the company's assets. That conduct occurred approximately two years after this Court's decisions in *SEC* v. *Texas Gulf Sulphur Co., supra,* and *Heit* v. *Weitzen,* 402 F.2d 909 (2d Cir. 1968), *cert. denied,* 395 U.S. 903 (1969), construing Section 10(b) and Rule 10b-5. Surely by 1970 Persky had been given fair notice that his contemplated conduct was either forbidden by that Section and Rule or was approaching proscription by them. And where, as here, a statute as applied to a

particular defendant's conduct is not vague, "it is irrelevant that it may be vague in other contexts with respect to other conduct." *Smith* v. *Goguen,* 415 U.S. 566, 585-86 (1974) (White, *J.*, concurring). "One to whose conduct a statute clearly applies may not successfully challenge it for vagueness." *Parker* v. *Levy, supra,* 417 U.S. at 756.* Moreover, in the area of business regulation, "it [is hardly] unfair to require that one who deliberately goes perilously close to an area of proscribed conduct shall take the risk that he may cross the line." *Boyce Motor Lines, Inc.* v. *United States,* 342 U.S. 337, 340 (1952).

POINT II

Judge Wyatt correctly instructed the jury that to convict they must find that Persky's alleged misconduct was "in connection with" the purchase or sale of Microthermal stock.

Persky challenges the correctness of Judge Wyatt's jury instruction explicating the "in connection with" element of the Rule 10b-5 offense alleged. That instruction, in pertinent part, provided:

> "And the third essential element is that the defendant, Mr. Persky, engaged in this conduct in connection with the purchase or sale or both of shares of Micro.

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* The Supreme Court has carved out an exception to this rule, not applicable here, in the first Amendment area of constitutionally protected expression. There, under certain circumstances, attacks have been permitted "on overly broad statutes with no requirement that the person making the attack demonstrate that his own conduct could not be regulated by a statute drawn with the requisite narrow specificity." *Dombrowski* v. *Pfister,* 380 U.S. 479, 486 (1965).

> Now, the Government need not show that the defendant, Mr. Persky, or any of the others named, bought or sold themselves shares of Micro or participated in such transactions. It is sufficient if the Government shows that from the period between July 1, 1970, and March 31, 1971, there were purchases or sales or both of shares of Micro, and that the device or scheme employed or act or practice was of a sort that would cause reasonable investors to rely thereon, and in connection therewith so relied to purchase or sell shares of Micro (Tr. 1297-98)."

Persky contends that it was error to permit the jury to find that the "in connection with" element of the offense could be satisfied absent a finding that Persky or one of the other named defendants either (1) purchased or sold stock of Microthermal, or participated somehow in such transactions, during the time of the alleged misconduct; or (2) intended by that misconduct to influence the market price of Microthermal stock. The contention is in error.

It is well settled that where an insider of a corporation whose stock is publicly traded issues corporate press releases through the financial media, and transmits notices to stockholders, which are knowingly and materially false, his conduct, without more, may bear a sufficient "connection with" the open market purchases and sales to constitute a violation of Section 10(b) and Rule 10b-5 thereunder. *SEC* v. *Koenig*, 469 F.2d 198, 201-02 (2d Cir. 1972); *SEC* v. *North American R. & D. Corp.*, 424 F.2d 63, 75-77 (2d Cir. 1970) (progress report to shareholders); *SEC* v. *Great American Industries, Inc.*, 407 F.2d 453, 456-58 (2d Cir. 1968) (en banc), *cert. denied*, 395 U.S. 920 (1969).

In its landmark case, *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 862 (2d Cir. 1968) (en banc), *cert. denied sub nom. Coates* v. *SEC*, 394 U.S. 976 (1969), this Court held:

> "Rule 10b-5 is violated whenever assertions are made, as here, in a manner reasonably calculated to influence the investing public, *e.g.*, by means of the financial media . . . if such assertions are false or misleading or are so incomplete as to mislead irrespective of whether the issuance of the release was motivated by corporate officials for ulterior purposes."

In explicating the language of Section 10(b) and Rule 10b-5 thereunder, this Court further said:

> "Congress when it used the phrase 'in connection with the purchase or sale of any security' intended only that the device employed, whatever it might be, be of a sort that would cause reasonable investors to rely thereon, and, in connection therewith, so relying, cause them to purchase or sell a corporation's securities. *There is no indication that Congress intended that the corporations or persons responsible for the issuance of a misleading statement would not violate the section unless they engaged in related securities transactions or otherwise acted with wrongful motives;* indeed, the obvious purpose of the Act to protect the investing public and to secure fair dealing in the securities markets would be seriously undermined by applying such a gloss onto the legislative language." *Id.* at 860 (emphasis added).

Here, as *Texas Gulf Sulphur* made clear, the "in connection with" requirement could be satisfied by the fact that "the public [was] purchasing and selling securities on the open market", *id.* at 882-83 (Moore, *J.*, dissenting), and Judge Wyatt properly so instructed the jury. That formulation comported with the by now conventional learning that while the "connection" element has been retained, "the common law requirement of privity has all but vanished from 10b-5 proceedings." *Mitchell* v. *Texas Gulf Sulphur Co.*, 446 F.2d 90, 101 (10th Cir.), *cert. denied*, 404 U.S. 1004

(1971); *accord, Shapiro* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 495 F.2d 228, 239 (2d Cir. 1974).

In *Heit* v. *Weitzen*, 402 F.2d 909, 913 (2d Cir. 1968), *cert. denied*, 395 U.S. 903 (1969), a private action for damages under Rule 10b-5 with facts remarkably similar to those of the instant case,* this Court held that there was no necessity for plaintiffs to allege or prove trading in the company's securities by defendant insiders or by the company itself contemporaneous with plaintiffs' purchases. This Court there went on to say:

> "[W]e conclude that plaintiffs have met the requirements of the 'in connection with' clause. It is reasonable to assume that investors may very well rely on the material contained in false corporate financial statements which have been disseminated in the market place, and in so relying may subsequently purchase securities of the corporation. The 'ulterior motive' present in the instant case—the concealment of the fraud from the government—is irrelevant, since the false information was circulated to a large segment of the investing public. It is impossible to isolate the particular 'fraudulent' acts and consider them as directed toward the government alone." *Id.*

Accord, SEC v. *Koenig, supra; SEC* v. *North American R. & D. Corp. supra; SEC* v. *Great American Industries, Inc., supra; Financial Industrial Fund, Inc.* v. *McDonnell Douglas Corp.*, CCH FED. SEC. L. REP. ¶ 93,004 (D. Col. 1971);

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* In *Heit*, plaintiffs had purchased on the open market, from non-defendant third parties, convertible debentures and common stock of a public company subsequent to that company's issuance of its annual report and certain press releases, and its filing of various documents with the SEC and the American Stock Exchange—all of which failed to disclose that a substantial amount of the company's income for the fiscal year 1964 derived from various overcharges on government contracts.

Sprayregen v. *Livingston Oil Co.*, CCH FED. SEC. L. REP. ¶ 92,272 (S.D.N.Y. 1968); *Fischer* v. *Kletz*, 266 F. Supp. 180, 193-94 (S.D.N.Y. 1967); *Freed* v. *Szabo Food Service, Inc.*, CCH FED. SEC. L. REP. ¶ 91,317 (N.D.Ill. 1964).

Persky further argues that even if Judge Wyatt properly articulated the law on this point, the government failed to prove that as a consequence of Persky's alleged misconduct anyone was, in fact, damaged or defrauded.* The argument is both legally and factually in error.

Given the pleadings and the government's theory of the case at bar, which rested primarily on the false and misleading statements contained in the press releases and notices to Microthermal stockholders, the government was required to prove, and did prove, that "in connection with" the purchase or sale of Microthermal stock, as defined above, the "defendant misrepresented or failed to disclose material facts . . . *knowing* that the facts represented were false or that he failed to disclose material facts." *United States* v. *Koenig*, CCH FED. SEC L. REP. ¶ 94,765, at 96,541 (S.D.N.Y. 1974) (emphasis in original).** Nothing rooted in law or reason required the government to establish in addition a specific intent on defendant Persky's part to affect the market price of Microthermal stock, or to establish that the misconduct alleged in fact did affect the market price of that stock. *Id; SEC* v. *Texas Gulf Sulphur Co.*, *supra*, 401 F.2d at 860. See also *United States* v. *Schaefer*, 299 F.2d 325, 629 (7th Cir.), *cert. denied*, 370 U.S. 917 (1962). Indeed, in a criminal prosecution under Rule 10b-5 the government is not required to prove that any adverse effect, in-

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* This argument is set forth in Point III of Persky's brief on appeal.

** One test of materiality under Rule 10b-5 "is whether 'a reasonable man would attach importance [to the fact misrepresented] in determining his choice of action in the transaction in question.'" *List* v. *Fashion Park, Inc.*, 340 F.2d 457, 462 (2d Cir.), *cert. denied sub nom. List* v. *Lerner*, 382 U.S. 811 (1965).

tended or otherwise, was caused by the prohibited conduct in issue (here, the making of untrue statements of material facts). As this Court has said "we see no more reason for requiring proof of actual (as distinguished from potential) injury in a criminal prosecution [under Rule 10b-5] than in a suit for an injunction in a securities fraud case." *United States* v. *Peltz*, 433 F.2d 48, 53 (2d Cir. 1970), *cert. denied*, 401 U.S. 955 (1971); *accord*, *United States* v. *Jones*, 380 F. Supp. 343, 345 (D.N.J. 1974).

Moreover, even if proof of actual injury was required, the government readily met that burden. Lloyd Albin, after receiving two press releases and a notice of stockholders meeting, all of which falsely represented that there was or would remain in Microthermal $375,000 in cash or cash items, purchased an additional 1,000 shares of Microthermal stock, at $2.50 per share, on November 30, 1970. He testified that he would not have purchased those additional shares, which thereafter became worthless, had he known the truth of Microthermal's financial condition. It can hardly be gainsaid that others who purchased throughout this period would not have done so had they likewise been provided with the truth.*

Finally, Persky's asserts in error that in a criminal prosecution, as here, the government's burden to establish the "in connection with" element of the alleged offense is somehow different and more stringent than that which

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* The government conclusively established through the testimony of at least three witnesses (Tr. 177-78, 384, 763), as well as documentary evidence including the transfer sheets of the transfer agent (GX 64, 65), that the stock of Microthermal was publicly traded in the over-the-counter market throughout the relevant period. Persky's suggestion otherwise is specious. In any event, it is well settled that the proscriptions of Section 10(b) and Rule 10b-5 apply not only to open market purchases and sales but to face-to-face transactions as well. *Supt. of Insurance* v. *Bankers Life & Cas. Co.*, *supra*, 404 U.S. at 10.

obtains in civil proceedings. We have found no legal authority warranting such a distinction. As was said in *United States* v. *Clark,* 359 F. Supp. 128, 130 (S.D.N.Y. 1973):

> "As a result of *Texas Gulf* and *Heit,* the Court of Appeals for this Circuit has announced its interpretation on the 'in connection with' language of § 10(b) and Rule 10b-5, and has applied that interpretation both in an S.E.C. injunction action and in private damage actions. In my view, there is no reasonable basis for holding that some different interpretation should apply to a criminal action."

See also *United States* v. *Peltz, supra,* 433 F.2d at 53 (Friendly, *J.*).

CONCLUSION

The judgment of conviction should be affirmed.

Respectfully submitted,

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AFFIDAVIT OF MAILING

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

JOHN C. SABETTA, being duly sworn, deposes and says that he is employed in the office of the United States Attorney for the Southern District of New York.

That on the 28th day of May, 1975 he served 2 copies of the within brief by placing the same in a properly postpaid franked envelope addressed:

Robert S. Persky, Esq.
One Rockefeller Plaza
New York, N.Y. 10020

And deponent further says that he sealed the said envelope and placed the same in the mail drop for mailing at the United States Courthouse, Foley Square, Borough of Manhattan, City of New York.

John C. Sabetta

Sworn to before me this
28th day of May, 1975

Jeanette Ann Grayeb

JEANETTE ANN GRAYEB
Notary Public, State of New York
No. 24-1541575
Qualified in Kings County
Commission Expires March 30, 1977